

## Retention of title clause created a trust, not a charge

- 1 The High Court of Australia has breathed new life into retention of title ('ROT') clauses. By a four-to-one majority, the Court has upheld the effectiveness of an agreement providing for the proceeds of sale of manufactured goods to be *held in trust*, thereby securing the manufacturer's indebtedness to the seller. The fact that the ROT clause created a trust, rather than a charge, meant it was effective despite not being registered under the Australian equivalent of the Companies Act.
- 2 In the case of *Associated Alloys v ACN 001 452 106*, Associated Alloys ('Seller') sold steel to a customer ('Buyer') subject to a ROT clause. The critical provision in the clause stated:

'In the event that the [Buyer] uses the goods/product in some manufacturing or construction process of its own or of some third party, then the [Buyer] shall hold such part of the proceeds of such manufacturing or construction process as relates to the goods/product in trust for the [Seller]. Such part shall be deemed to equal in dollar terms the amount owing by the [Buyer] to the [Seller] at the time of the receipt of such proceeds.'
- 3 The Buyer used the steel in the manufacture of pressure vessels, heat exchangers, and columns ('steel products'). It was agreed that the Seller had not retained title to the steel products since the steel it had supplied was no longer ascertainable in the products; the steel products were physically different property. The steel products were sold to a third party, with the third party making payments to the Buyer. The question for the Court to consider was whether the Seller had priority over those payments *by virtue of* the provision set out above.
- 4 The Judge at first instance, and the Court of Appeal, had held that the clause insofar as it operated to confer on the Seller a *proprietary interest* in the proceeds, was a charge over book debts and was *void for non-registration*. The majority in the High Court rejected that reasoning. In the majority's view, there is a critical distinction to be drawn between trusts and charges.
- 5 In drawing the distinction in relation to the particular clause in question, the Court noted that effect had to be given to the legal relationship the parties had entered into. On that basis, the Court held that the ROT clause created a trust. The fact that the amount subject to the trust was determined by reference to the amount that the Buyer owed the Seller did not reduce the importance of this characterisation.
- 6 In the end, and despite substantially upholding the Seller's arguments as to the effect of the clause, the Court dismissed the Seller's appeal *on an evidential ground*. The Seller had not *adduced evidence* to show a link between the steel it had supplied and the payments for products supplied to the third party. This gap in the evidence meant that the Seller's appeal failed.
- 7 However, despite the Seller's ultimate failure, the majority's decision strengthens a seller's position and consequently could alter the balance where sellers and secured creditors compete for priority.

# Photocopiable worksheet 9.3

Complete these six complex sentences from Reading 2 using the words in the boxes.

- 1 By ..... four ..... one ..... , the ..... has ..... the ..... of ..... agreement ..... for ..... proceeds ..... sale ..... manufactured ..... to ..... held ..... trust, ..... securing ..... manufacturer's ..... to ..... seller.

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majority of of providing the the the thereby to upheld

- 2 It ..... agreed ..... the ..... had ..... retained ..... to ..... steel ..... since ..... steel ..... had ..... was ..... longer ..... in ..... products; ..... steel ..... were ..... different ..... .

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- 3 ..... Judge ..... first ..... , and ..... Court ..... Appeal, ..... held ..... the ..... insofar ..... it ..... to ..... on ..... Seller ..... proprietary ..... in ..... proceeds, ..... a ..... over ..... debts ..... was ..... for ..... .

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non-registration of operated that the the the the void was

- 4 ..... drawing ..... distinction ..... relation ..... the ..... clause ..... question, ..... Court ..... that ..... had ..... be ..... to ..... legal ..... the ..... had ..... into.

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- 5 In ..... end, ..... despite ..... upholding ..... Seller's ..... as ..... the ..... of ..... clause, ..... Court ..... the ..... appeal ..... an ..... ground.

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- 6 However, ..... the ..... ultimate ..... , the ..... decision ..... a ..... position ..... consequently ..... alter ..... balance ..... sellers ..... secured ..... compete ..... priority.

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majority's seller's Seller's strengthens the where